No. 8409.

IN THE

UNITED STATES CIRCUIT COURT OF APPEALS

IN AND FOR THE

NINTH CIRCUIT

J. N. HENDRICKSON,
Complainant,

vs.

EL CAMINO OIL COMPANY, LTD., a corporation,
Respondent.

STATE OF CALIFORNIA,
Creditor and Appellant,

vs.

H. A. MEEK, as Receiver of the El Camino Oil Company, Ltd., a corporation,
Receiver and Appellee,

F. R. KENNEY and L. W. WICKES,
Creditors and Appellees.

APPELLANT'S OPENING BRIEF

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APPELLANT'S OPENING BRIEF

I. STATEMENT OF JURISDICTION

This is an appeal from an order (Tr. pp. 84-87) of the District Court of the United States, Southern District of California, Central Division, determining the existence and relative priority of liens of the appellant, the State of California, and of the appellees F. R. Kenney and L. W. Wickes, respectively, upon property in the possession of the appellee

H. A. Meek, as receiver of the respondent El Camino Oil Company, Ltd.

Said receiver was appointed in a suit commenced by a creditor, to conserve the assets of the debtor, the El Camino Oil Company, Ltd., for the benefit of all creditors, through orderly liquidation. The usual notice was given requiring the presentation of claims. Two individual claimants, F. R. Kenney and L. W. Wickes, (hereinafter referred to as the individual claimants or contract creditors), presented a joint claim setting up their claim based upon two promissory notes executed by the debtor corporation and secured, respectively, by a chattel mortgage and a deed of trust upon certain property of said corporation. The State of California presented its claim for taxes and penalties thereon, secured by a lien therefor as provided by the tax statute, upon all of the property of said debtor corporation. (See opinion of District Court, Tr. p. 76, which opinion is adopted (Tr. p. 87) as a part of the findings and conclusions of said court).

Thereafter, the State of California filed in said receivership proceeding its petition for an order to show cause why its claim for taxes should not be allowed as a preferred claim and as a lien claim paramount to the claims and liens of other creditors of the respondent corporation. (Tr. pp. 3-4.) An order to show cause was duly issued pursuant to said petition. (Tr. pp. 5-6.) H. A. Meek, as receiver for said El Camino Oil Company, Ltd.,

duly filed his answer to said order to show cause, (Tr. pp. 7-13) and the matter was submitted to said district court upon a stipulated statement of facts (Tr. pp. 14-22) and exhibits attached thereto (Tr. pp. 22-43); as supplemented by a further stipulation as to additional facts (Tr. pp. 44-47), with exhibits attached thereto (Tr. pp. 48-74.) By this further stipulation the attorneys for the aforesaid appellees F. R. Kenney and L. W. Wickes joined in said stipulation and also in the original stipulation of facts hereinabove referred to (Tr. p. 47), and thereby submitted to the jurisdiction of said district court under said petition and order to show cause.

Said district court rendered and filed its memorandum of decision (Tr. pp. 75-83), pursuant to which the order herein appealed from was made. (Tr. pp. 84-87.) Said order adopted said stipulations and said memorandum of decision as the findings and conclusions of law of the court. (Tr. p. 87.) A petition for rehearing (Tr. pp. 88-91) was denied (Tr. p. 92), and the state of California thereupon filed in said district court its petition for appeal (Tr. pp. 93-94), supported by assignments of error (Tr. pp. 96-101), whereupon said district court duly made its order allowing said appeal to this court. (Tr. pp. 94-95.)

Under the foregoing pleadings and facts, the jurisdiction of said district court in said receivership proceeding is sustained by section 24, sub-

division (1), of the Judicial Code. (28 U. S. C. A. Sec. 41). Having thus taken jurisdiction of said proceeding, the district court had jurisdiction to decide all questions incident to the preservation, collection, and distribution of the assets of the debtor.

See *Riehle* vs. *Margolies,* 279 U. S. 218, 49 S. Ct. 310, 312, 73 L. Ed. 669 (1929).

The jurisdiction of this court, upon appeal, to review said order, is sustained by sections 128 and 129 of the Judicial Code (28 U. S. C. A. Secs. 225, 227).

II. STATEMENT OF THE CASE

A. The Facts

As has been stated, the facts were stipulated to in detail, and are set forth in the transcript of record. (Tr. pp. 14-74.) In its order (Tr. p. 87), the court adopted said stipulations and its memorandum of decision (Tr. pp. 75-83), as its findings of fact and conclusions of law. In giving a brief summary of the facts pertinent upon this appeal reference will therefore be made to both said stipulations and said memorandum of decision.

During the quarter years ending March 31, June 30, and September 30, 1930, and March 31, 1931, respectively, the El Camino Oil Company, Ltd., became indebted to the state of California for taxes on account of motor vehicle fuel distributed by

said company during said periods. Said taxes were assessed pursuant to the provisions of the California Motor Vehicle Fuel License Tax Act (Calif. Stats, 1923, p. 571, as amended, and Calif. Stats. 1927, p. 1565). None of said taxes was paid prior to the respective dates of delinquency, and a 10 per cent penalty was thereupon added to each of said taxes as provided in said act, and was entered upon the assessment roll by the Controller of the State of California. (Tr. pp. 14-16, 75.) Since May 15, 1930, certain sums have been paid to the State of California by said El Camino Oil Company, but there remains a large balance on account of each of said quarterly taxes. (Tr. pp. 16-17.)

On June 6, 1930, said El Camino Oil Company executed and delivered to the appellees F. R. Kenney and L. W. Wickes a promissory note in the amount of $10,000, and at the same time executed and delivered to said appellees a chattel mortgage to secure the payment of said note. (Tr. pp. 22-28, 75-76.) On June 7, 1930, said company executed and delivered to said individual creditors its promissory note in the amount of $80,000, and at the same time executed and delivered a deed of trust to secure the payment of said note. (Tr. pp. 28-41, 76.) Each of said encurbrances was recorded in the official records of the county recorder's office of the county of Los Angeles, California, on June 10, 1930. (Tr. pp. 18, 76.) The consideration for said notes was a then existing

indebtedness by said company to said appellees for crude oil furnished said company by said appellees in an amount not then ascertained but which was later determined to be $78,046.60. (Tr. pp. 18-19, 75-76.)

The deed of trust purportedly transferred in trust two "parcels." The first was a parcel of land owned by the El Camino Oil Company, and particularly described in said deed. (Tr. p. 28.) The second was said company's right, title and interest, *as lessee,* in a certain lease covering the premises upon which was and is situated the oil refinery of said El Camino Oil Company. Said deed of trust after particularly describing said Parcel II, further provided

> "that all that certain oil refinery located upon Parcel II above described and all that certain bulk plant located upon Parcel I above described, including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills, and fractionating towers now situated upon the above described premises, or either of them, in whatever manner affixed or attached to either of said parcels of real property, are and shall be deemed to be real property and expressly included in the above grant, transfer and assignment."

Said instrument was executed by said El Camino Oil Company, by the signatures of its president and secretary, who likewise acknowledged before a notary public "that such corporation executed

the same." (Tr. pp. 38-39.) Said trust deed was not, however, accompanied by the affidavit of all or any of the parties thereto that it was made in good faith and without any design to hinder, delay or defraud creditors. (Tr. pp. 38-39.) Nor was there ever any transfer of possession of any of the property described in said trust deed, to either the trustee or the beneficiary named therein. In other words, said El Camino Oil Company was continuously in possession of all of said property at all times mentioned until possession of the same was taken by the receiver. (Tr. pp. 46-47.)

Said El Camino Oil Company was not at any time, and is not now, the owner of the real property described as Parcel II in said deed of trust, but its only interest in said premises was and is under and by virtue of a certain lease, a copy of which is set forth in the transcript of record. (Tr. pp. 44, 48-68.) At the time said lease was made, said premises were vacant and unimproved. Thereafter, however, and prior to the date of any of the distributions for which the aforesaid taxes were levied, said oil company erected and installed thereon, its refinery plant and equipment. The lease provided that upon the expiration of its term the lessee should yield up the premises to the lessor in as good condition as the same were at the commencement of said term, reasonable use and wear thereof excepted. However, the lessor expressly covenanted

> "That the boilers, engines, machinery, tanks, vats, stills, pipes, equipment and fixtures, and all

personal property erected on said leased premises by the lessee may be removed by the lessee at the termination of this lease, or any extension thereof, even though the same may be attached to said premises: Provided, the lessee shall not then be in default in the performance of the covenants hereof; and provided further, that the removal of any such property shall be effected before the expiration of said term, or any extension thereof, and all damages caused to said premises by such removal shall be repaired by the lessee on or before the expiration of said term." (Tr. p. 54.)

All of the property now in the possession of the receiver was at all times during which the aforesaid taxes accrued, owned by said company or in the possession and use of said company under purchase contracts reserving title in the vendor for the purpose of security until payment in full of the purchase price. (Tr. p. 45.) Since the inception of the receivership, all balances due on said contracts have been paid by the receiver from moneys received under a lease of the refinery of the said El Camino Oil Company, which lease was made by the receiver. (Tr. p. 46.)

B. The Questions Involved on This Appeal

Upon the foregoing facts, and pursuant to the proceedings had as heretofore related, the district court ruled that the State of California had a valid and existing claim against the receivership estate for taxes in the sum of $252,420.29, on account of

gasoline sold and delivered by the El Camino Oil Company, Ltd., and for penalties thereon in the sum of $33,604.91. This entire claim was declared to be a lien upon all of the property of said company, attaching as of the time of the sale and distribution of gasoline by said company on account of which said taxes were imposed, and remaining until the license tax for which said lien was imposed is paid or the property sold for the payment thereof. (Tr. pp. 84-85.) No appeal has been taken from this portion of the district court's order.

The district court further held that the appellees F. R. Kenney and L. W. Wickes, also had a valid and existing claim against the receivership estate, in the sum of $78,046.60, together with interest thereon at the rate of 7 per cent per annum, compounded quarterly from the thirty-first day of May, 1932, and that said claim is secured by the aforesaid chattel mortgage of June 6, 1930, and deed of trust of June 7, 1930, which were specifically declared to be "a valid and existing lien upon the property described in said chattel mortgage and deed of trust." (Tr. p. 85.) The State of California has appealed from this portion of said order. First, it contends that no portion of the claim of said appellees is or was at the commencement of the receivership proceedings herein, secured by said chattel mortgage. (See Assignment of Error, II; Tr. p. 97.) This contention is based upon the ground that the $10,000 note which was secured by said chattel mortgage, was fully satisfied by the

accounting had between the parties thereto, subsequent to the execution of said instrument, by which accounting the amount of the indebtedness of the El Camino Oil Company to said individual creditors was ascertained to have been $78,046.60 only, or, in other words, in an amount less than that of the note purportedly secured by the deed of trust, which was of later date than either the $10,000 note or chattel mortgage.

The State of California further contends that, as to the property described as Parcel II in said deed of trust, namely, the interest of said El Camino Oil Company, as lessee, in certain real property particularly described therein, said instrument did not create a valid lien as against the State of California. (See Assignment of Error, IX; Tr. p. 98.) This contention is based upon the ground that the property described in said deed of trust as Parcel II is personalty rather than realty, and said trust deed was not executed in the manner required for mortgages of personal property.

Having held that both the State of California as tax claimant, and said contract creditors, held valid and existing liens upon the property in the possession of the receiver, the district court held that the lien of the State of California for the unpaid balance of the claim of said state for license taxes due on account of gasoline sold and delivered by the El Camino Oil Company, Ltd., during the first period involved, viz, prior to and including March 31, 1930, was prior and paramount to the lien of

said individual creditors under the aforesaid chattel mortgage and deed of trust. (Tr. p. 86.) No appeal has been taken from this portion of said order.

As to the portion of the claim of the State of California which was for license taxes due on account of gasoline sold and delivered by the El Camino Oil Company during the second period involved, viz, subsequent to the thirty-first day of March, 1930, but prior to and including the tenth day of June, 1930, the district court held that the lien securing said tax claim was prior and paramount to the aforesaid contract lien of the appellees, Kenney and Wickes. (Tr. p. 56.) No appeal has been perfected from this portion of said order. However, the district court did *not* order that the state's lien for *penalties* which subsequently were added to the assessment roll on account of the failure to pay said taxes which accrued during this second period, was prior and paramount to the lien of said contract creditors. The State of California contends that although said penalties were not added upon the assessment roll until after said chattel mortgage and deed of trust were recorded, on June 10, 1930, the *lien* for said penalties attached, as did the lien for the taxes to which said penalties were so added, as of the date of the delivery of the gasoline on account of which said taxes accrued, to wit, *prior* to June 10, 1930. (See Assignments of Error V and XI; Tr. pp. 97, 99.)

As to the portion of the claim of the State of California which was for license taxes due on account of gasoline sold and delivered by the El Camino Oil Company during the third period involved, viz, subsequent to the tenth day of June, 1930, the district court held that the lien of the state, for both said taxes and the penalties thereon, was subsequent and inferior to the lien of said individual creditors under said chattel mortgage and deed of trust. (Tr. p. 87.) The State of California contends that, even if it be assumed that the claim of said contract creditors was secured by said chattel mortgage, and that said deed of trust is valid as against the State of California, the lien securing the claim of the State of California, in its entirety, was nevertheless prior and paramount to any such lien created by said chattel mortgage (See Assignment of Error VI; Tr. pp. 97-98), and said deed of trust. (See Assignment of Error XII; Tr. p. 99.) In other words, it is contended that, in any event, *the state's tax lien is paramount to even antecedent contract liens.*

Briefly, then, the questions involved in this appeal are as follows:

1. Where a debtor, who is indebted to a creditor in an unascertained amount, satisfies said unliquidated debt by the execution, on one day, of a $10,000 note secured by a chattel mortgage, and by the execution, on the following day, of an $80,000 note secured by a deed of trust of even date, and

it is thereafter ascertained, by an accounting between said parties that the amount of the indebtedness is and was in fact only $78,046.60, must the court, in applying the credit in the amount of $11,-853.40 to which the debtor is thus entitled, first apply said credit to the satisfaction of said $10,000 note secured by said chattel mortgage?

2. Where a debtor, in order to secure its promissory note, grants, conveys, transfers, assigns, and sets over, in trust, all of his right, title and interest *as lessee* in and to certain real property, and there is no transfer of possession of said leasehold estate, nor is the instrument by which such assignment in trust is made, executed and recorded in the manner required for the execution and recording of mortgages of *personal property,* is such encumbrance valid as against the State of California as a tax creditor of said debtor?

3. Where a motor vehicle fuel tax accrues and becomes a lien upon the property of the distributor as distributions of such fuel are made (although the tax is not assessed until a later date, after which date a penalty is added to the tax upon the assessment roll, for failure to pay said tax before the delinquency date), does the lien for the *penalty* on said tax attach as of the date of the distribution of said fuel, as did the lien for the taxes to which said penalties were added?

4. Where, pursuant to the provisions of the California Motor Vehicle Fuel License Tax Act, taxes

accrue and become a lien upon the property of the tax debtor subsequent, in point of time, to the time when instruments creating private contract liens on certain property of said debtor are recorded, is said tax lien *paramount* to said antecedent contract liens?

It is apparent, of course, that if this court holds, as appellant believes it must, that the entire lien of the State of California is paramount to any and all liens which the individual creditors may have upon the property of the debtor company, then a decision upon the first three questions stated above would not be necessary in order to require a reversal of the order of the district court. For it is immaterial what valid liens the individual creditors may have, and it is not necessary to determine when the lien for penalties attached, if the state's lien is, in any event, paramount to even *antecedent* contract liens which are *valid* as against the state.

III. SPECIFICATIONS OF ERROR

The foregoing questions will each be considered separately in the order mentioned. In presenting said questions, appellant relies upon the following assignments of error:

Point One, Assignment II, (Tr. p. 97);

Point Two, Assignment IX, (Tr. p. 98);

Point Three, Assignments V and XI, (Tr. pp. 97, 99);

Point Four, Assignments VI and XII, (Tr. pp. 97-98, 99).

IV. ARGUMENT OF APPELLANT

A. Point One

The district court erred in ordering that the claim of F. R. Kenney and L. W. Wickes, or any portion thereof, is secured by a chattel mortgage dated the sixth day of June, 1930, executed by El Camino Oil Company, Ltd., and recorded in the office of the county recorder of Los Angeles County the tenth day of June, 1930.

This point relates to Assignment of Error No. II. (Rep. Tr., p. 97.)

As has been noted, on June 6, 1930, the El Camino Oil Company, the respondent herein, executed and delivered to the appellees Kenney and Wickes, its $10,000 note, purportedly secured by a chattel mortgage of even date. (Tr. pp. 22-28, 75-76.) Then, on June 7, 1930, an additional promissory note was executed in favor of said appellees in the amount of $80,000. This note was purportedly secured by a deed of trust of the same date. (Tr. pp. 75-76, 18, 38.) At the time said notes were executed the exact balance due individual creditors by the oil company was not known, but said notes were made in the aforesaid amounts in order to amply cover the indebtedness which would thereafter be fixed by said parties. Thereafter, pursuant to this understanding, it was ascertained that the correct amount of the indebtedness by the respondent oil company to said individual creditors was, at all of said times, in the amount of $78,046.60, only. (Tr. pp. 18 to 19.) Thus the

respondent oil company was entitled to a credit of $11,953.40 upon the obligations evidenced and secured by the aforementioned documents. The contention of the State of California is that said credit must first be applied by the court to the payment of said $10,000 note secured by said chattel mortgage, thus, in effect, leaving no such obligation at the time of the receivership proceeding herein.

Section 1479 of the California Civil Code provides as follows:

> "Application of general performance. Where a debtor, under several obligations to another, does an act, by way of performance, in whole or in part, which is equally applicable to two or more of such obligations, such performance must be applied as follows:
>
> One. If, at the time of performance, the intention or desire of the debtor that such performance should be applied to the extinction of any particular obligation, be manifested to the creditor, it must be so applied.
>
> Two. If no such application be then made, the creditor, within a reasonable time after such performance, may apply it toward the extinction of any obligation, performance of which was due to him from the debtor at the time of such performance; except that if similar obligations were due to him both individually and as a trustee, he must, unless otherwise directed by the debtor, apply the performance to the extinction of all such obligations in equal proportion; and an application once made by the

creditor cannot be rescinded without the consent of the debtor.

Three. If neither party makes such application within the time prescribed herein, the performance must be applied to the extinction of obligations in the following order; and, if there be more than one obligation of a particular class, to the extinction of all in that class, ratably:

1. Of interest due at the time of the performance.
2. Of principal due at that time.
3. Of the obligation earliest in date of maturity.
4. Of an obligation not secured by a lien or collateral undertaking.
5. Of an obligation secured by a lien or collateral undertaking."

It is uncontroverted, in the principal case, that neither party to the above mentioned notes made any particular application of the credit to which the debtor oil companies became entitled by reason of the accounting, had as aforesaid. It is therefore necessary for the *court* to apply said credit in accordance with the provisions of paragraph three of said section 1479. That said section relates to payments by way of "credits" to which the debtor is entitled, as well as to any other payments, is settled in the case of *McColgan* vs. *Sockolov,* 192 Cal. 171 (1923). There, it was squarely held that where the maker of several notes is entitled to credit on said notes or some of them, for services performed, the

credit should be applied against the notes bearing the *earliest date*, in accordance with the method outlined by the aforesaid code section 1479.

Applying said code section and said decision to the principal case, it is evident that the credit to which the respondent oil company was entitled must first be applied upon the $10,000 note, that being the obligation earliest in date of maturity. Accordingly, it must be held that there is no sum due on account of said $10,000 note secured by said chattel mortgage. The district court, therefore, erred in ordering that the claim of said contract creditors is now secured by said chattel mortgage. Its order should be modified accordingly.

B. Point Two

Said district court erred in ordering that the deed of trust executed June 7, 1930, by the El Camino Oil Company, created and constitutes a valid and existing lien, as against the State of California, upon the property described in said deed of trust as Parcel II.

This point relates to the error assigned as Number IX, in the assignment of errors filed herein. (Tr. p. 98.)

Briefly summarized, the proposition here presented by the appellant is that, whatever may be the effect of the deed of trust heretofore referred to, as between the parties thereto, it was of no effect as against the State of California, as to the property described therein as Parcel II, because said

state did not have notice of said encumbrance, either actual or constructive. The lack of *actual* notice is not disputed. The state contends that it did not receive any *constructive* notice of any encumbrance upon said property described as Parcel II, because there was neither any transfer of possession of said property, nor did the parties to said deed of trust comply with the laws of the State of California relating to the execution and recordation of instruments creating encumbrances upon personal property. The validity of this contention of the State will more clearly appear from the following argument.

By said trust deed the El Camino Oil Company as trustor conveyed to the trustee, as Parcel I, a certain parcel of land in the county of Los Angeles, State of California. (Tr. p. 28.) Continuing, said instrument provided that the trustor also granted, conveyed, transferred, assigned and set over to the trustee, in trust with power of sale, "all that property in the county of Los Angeles, State of California, described as:

> "All Trustor's right, title and interest *as Lessee,* in and to that certain written lease dated September 16, 1929, between Matilda E. Richer, Lessor, and El Camino Oil Company, a corporation, Lessee, pertaining to and covering
>
> Parcel II: The West Five (5) acres of the North Fourteen (14) acres of the East Fifty-five (55) acres of the South Half ($S\frac{1}{2}$) of the Northwest Quarter ($NW\frac{1}{4}$) of Section 8.

Township 3 South, Range 11 West, San Bernardino Base and Meridian.

which said lease was recorded on the 24th day of September, 1929 in Book 9300, page 229 of Official Records in the office of the County Recorder of Los Angeles County, State of California, including Trustor's right under said lease to purchase said premises upon the terms and conditions set forth in said lease.

"Said grant, transfer and assignment of said Trustor's interest, *as Lessee,* in and to said lease is hereby made to said Trustee upon the express understanding and agreement between Trustor and Trustee that Trustee is not to be liable upon any of the covenants, obligations and requirements of said lease.

"It is expressly understood and agreed that all that certain oil refinery located upon Parcel II above described and all that certain bulk plant located upon Parcel I above described, including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills, and fractionating towers now situated upon the above described premises, or either of them, in whatever manner affixed or attached to either of said parcels of real property, are and shall be *deemed to be* real property and expressly included in the above grant, transfer and assignment." (Italics ours; Tr. pp. 29-30.)

It is undisputed that the trustor, the respondent oil company herein, did not own any interest in said parcel of real property except such interest as it had

as lessee. (Tr. p. 44.) In any event, the trustor did not, by said trust deed, purport to *transfer* any interest other than that which it had *as lessee.*

It is well established that a leasehold interest is merely personal property, and the rules relating to transfers of personal property apply to transfers of such leasehold interests. Thus in *J. S. Potts Drug Company* vs. *Benedict,* 156 Cal. 322, at 327, (1909), it was held that an *assignment* of a leasehold interest, being governed by the rules applicable to personal property, passed title immediately upon the agreement being made, no delivery of possession being necessary. Therefore, where the premises were destroyed by fire, before the assignee was placed in possession, said assignee was nevertheless liable for the price.

So, also, in *Summerville* vs. *Stockton Milling Co.,* 142 Cal. 529 at 537 (1904), it was held that a leasehold estate, being personal property, is not subject to the lien of a judgment as upon real property. Therefore, it was held that an antecedent judgment lien was not paramount to a later dated chattel mortgage of a crop growing upon the leased land there in question.

On principle then, there can be no question but that the parties to said trust deed were required to comply with the provisions of law relating to the mortgaging of *personal property* in order that their encumbrance of the leasehold interests of said respondent oil company might be valid as against

third persons. This they did not do, either by an actual transfer of possession, pursuant to section 3440 of the California Civil Code, or by executing and recording said instrument in compliance with the provisions of section 2957 of said Civil Code.

Said section 3440 specifically provides that:

> "Every transfer of personal property, other than a thing in action * * * and every lien thereon, other than a mortgage, when allowed by law * * * is conclusively presumed if made by a person having at the time the possession or control of the property, and not accompanied by an immediate delivery, and followed by an actual and continued change of possession of the thing transferred, to be fraudulent, and therefore void, against those who are his creditors while he remains in possession, * * * and against any persons on whom his estate devolves in trust for the benefit of others than himself, and against purchasers or encumbrancers in good faith subsequent to the transfer * * *."

It is undisputed that there was no actual transfer of possession of any of the property described in said deed of trust. (Tr. pp. 46-47.)

Said section 2957, at all times herein mentioned, provided as follows:

> "A mortgage of personal property is void as against creditors of the mortgagor and subsequent purchasers and encumbrancers of the property in good faith and for value, unless:
>
> 1. It is accompanied by the affidavit of all the parties thereto that it is made in good faith

and without any design to hinder, delay, or defraud creditors;

2. It is acknowledged or proved, certified, and recorded in like manner as grants of real property."

Executing and recording a mortgage in compliance with the provisions of said section is a substitute for the transfer of possession as required by said section 3440. (See *Wolpert* vs. *Gripton,* 213 Cal. 474 (1931).) While said deed of trust herein was in fact recorded, it is undisputed that it was *not* accompanied by the affidavit of all or of any of the parties thereto that it was made in good faith and without any design to hinder, delay or defraud creditors. By the express terms of said section 2957, then, said deed of trust is void as against the lien claim of the State of California, as a tax creditor of the trustor, the El Camino Oil Company.

In support of this conclusion based upon principle, see *Farmers State Bank* vs. *Scheel,* 214 Pac. 825 (Wash. 1923). There it was squarely *held* that the *assignment of a lease to secure an indebtedness, is a chattel mortgage and is subject to the statute requiring an affidavit of good faith and recording thereof.* See, also, *In re Empire Refining Company,* 1 Fed. Supp. 548 (1932), where the district court below, per Judge James, held that a chattel mortgage did not comply with the provisions of said section 2957 relating to the affidavit of good

faith. The files in said case disclose that the property there purportedly mortgaged was a *gasoline refinery located upon leased property.* Thus the court was required to held that the property in question was *personal property,* in holding that the mortgage thereof was subject to the provisions of said section 2957. Similarly, in the principal case, it must be held that the attempted encumbrance of the leasehold interest of the El Camino Oil Company, including its right *under said lease* to said gasoline refinery, plant, and equipment, was void as against the State of California, because it did not comply with the provisions of said section.

In this regard it should further be noted that said deed of trust, as has already been mentioned, provided that:

> "It is expressly understood and agreed that all that certain oil refinery located upon Parcel II above described and all that certain bulk plant located upon Parcel I above described, including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills, and fractionating towers now situated upon the above described premises, or either of them, in whatever manner affixed or attached to either of said parcels of real property, are and *shall be deemed to be* real property and expressly included in the above grant, transfer and assignment." (Tr. pp. 29-30; italics added.)

By this provision the parties to said instrument have attempted to convert into real property that

which even they recognized was in fact merely personal property. While such an agreement may be binding as between the parties thereto, it is not apparent how it can in anywise affect the rights of third parties without either actual or constructive notice thereof. On the contrary, it indicates a recognition even by the parties to said instrument, that the property in question was not *in fact,* real property. Therefore, in order to be valid as against the State of California, it should have been executed in the manner required by law for mortgages of personal property.

It thus appears that the appellees F. R. Kenney and L. W. Wickes do not now, nor did they at any time, have any lien upon said property described in said deed of trust as Parcel II, which was valid as against the State of California as tax creditor of said oil company. (As to the property described as Parcel I in said deed of trust, the State of California relies, for priority, upon its lien being paramount to even valid antecedent contract liens. This point will be considered hereinbelow.

It is therefore submitted that the district court erred in holding that the deed of trust dated June 7, 1930, created and constitutes a valid and existing lien, *as against the State of California* upon the property described in said deed of trust as Parcel II. The order of the district court should be modified accordingly.

C. Point Three

The District Court erred in ordering that said claim of F. R. Kenney and said L. W. Wickes constitutes a lien upon the property described in said chattel mortgage and deed of trust, prior and paramount to the lien of the state of California upon said property for penalties added to license taxes due on account of motor vehicle fuel sold and delivered by the El Camino Oil Co., Ltd., from and including the first day of April, 1930, to and including the tenth day of June, 1930.

This point relates to the errors assigned as Numbers V and XI in the assignment of errors filed herein. (Tr. p. 99.) Said assignment Number V relates specifically to the priority of the lien of the chattel mortgage over the lien for said penalties, and assignment Number XI relates specifically to the priority of the deed of trust over the lien for said penalties. However, since the same legal principles are involved as to each of said contract liens in this regard, said assignments have been consolidated herein for treatment as a single point.

Briefly, the proposition here presented by appellant is that when, subsequent to August 15, 1930, penalties were added to taxes which became delinquent on that date but which had accrued and become a lien from day to day during the second quarter of the year 1930, such penalties attached as a lien, the same as did the taxes to which said penalties were added, as of the date of the delivery of the gasoline on account of which said taxes accrued.

Therefore, as to the penalties which were added to any taxes which accrued on or before June 10, 1930, said penalties were, like the taxes to which they were added, secured by a lien which attached *prior in point of time* to the recording of the chattel mortgage and deed of trust of the individual claimants herein. Therefore the lien for said penalties clearly was paramount to the subsequent contract liens, if any, of said individual creditors.

As has been noted the court below held that the principal of the taxes assessed on the basis of the gasoline sold and delivered by the El Camino Oil Company subsequent to the thirty-first day of March, 1930, but prior to and including the tenth day of June, 1930, was secured by a lien which was prior and paramount to the contract lien of said individual creditors recorded on said tenth day of June, 1930. In so holding, the district court merely followed the express provisions of section 4 of the California Motor Vehicle Fuel License Tax Act. (Calif. Stats. 1923, p. 572; as amended by Calif. Stats. 1925, p. 659.) In 1930 said section 4 provided as follows:

> "Sec. 4. License taxes herein required to be paid shall be paid in quarterly installments to the state controller for the quarters ending December thirty-first, one thousand nine hundred twenty-three, and ending March thirty-first, June thirtieth, September thirtieth and December thirty-first in the year one thousand nine hundred twenty-four and each year thereafter.

> Said tax shall be a lien upon all of the property of the distributor. *It shall attach at the time of the delivery or distribution, subject to the tax,* shall have the effect of an execution duly levied against all property of the distributor, and shall remain until the tax is paid or the property sold for the payment thereof. The amount of such license tax becoming due during each such quarter shall be paid within thirty-five days after the end of the quarter for which the same is due, and if not paid prior thereto shall become delinquent at five o'clock p.m. on the forty-fifth day after the end of such quarter, and ten per cent penalty shall be added thereto for delinquency."

It is well settled that when a tax statute expressly designates the date as of which the tax lien shall attach, the lien comes into existence on that date regardless of the fact that certain further steps by the taxing authorities are necessary in order to fix the *amount* of the tax and render it *payable.*

> *County of San Diego* vs. *County of Riverside,* 125 Cal. 495, at 500 (1899);
> *City of Santa Monica* vs. *Los Angeles County,* 15 Cal. App. 710 (1911);
> 24 Cal. Jur. 218 to 219 ("Taxation," Sec. 208) (1936).

In other words, as the principle is summarized in 61 C. J. 924 to 925 ("Taxation," Sec. 1175):

> "While a statute which definitely fixes the date or time when the lien shall attach, does not do away with the necessity of the necessary steps to be taken before such lien can become

effectual, the lien dates back and takes effect by relation from the date or time fixed by the statute." (Citing the above cited California cases.)

In holding that the principal of the taxes assessed upon the basis of distributions by the El Camino Oil Company from April 1, 1930, to June 10, 1930, inclusive, became a lien upon said property as of the date of the distribution, notwithstanding the *amount* of said taxes was not fixed or assessed and did not become *payable* until subsequent to said tenth day of June, 1930, the court below was merely applying the foregoing principle.

Furthermore, the court below also held that the penalties which were added to the taxes assessed against said El Camino Oil Company pursuant to the provisions of the aforesaid section 4 of the tax statute were, as a part of the taxes to which they were added, a lien upon the property of said company. This ruling is squarely supported by the decision of this court in *State of California* vs. *Hisey,* 84 Fed. (2nd) 802, at 805 (9th C. C. A. 1936). For some reason, however, in determining the *time* as of which said lien for *penalties* attached, the court below chose to distinguish between the lien for the principal of the tax and the lien for said penalties. In other words, although the court had held, as above noted, that the lien for the *principal* of the tax assessed upon the basis of distributions during the period from

April 1, 1930, to June 10, 1930, attached as of the date of said distributions notwithstanding said taxes were not computed or assessed until thereafter, the court held that as to the *penalties* which were subsequently added to and became a part of said tax and were supported by the same lien which supported said tax, said lien securing the penalty did *not* attach as of the date of the distributions which were the basis for the assessments to which said penalties were added. It is submitted that in so ruling the district court erred. Clearly, the date specified in the foregoing section 4 as the date as of which the lien provided for by said section shall attach, relates to the *entire* lien created by said section. If, as this court has held, the penalties are a lien as a part of the tax to which they are added, it is difficult to perceive how it can reasonably be said that the lien for the principal of the taxes, on the one hand, attaches as of the date specified in the statute, while the lien for the penalties added to said taxes attaches as of some other date. Manifestly, the only sound construction of said section is that the entire lien created thereby attaches as of the date of the distributions which are subsequently made the basis for an assessment, which assessment may, in the event of delinquency, include an additional ten per cent thereon as a penalty. In other words, the *amount* of the tax lien will not be ascertained until it is determined whether said penalties must be added to said tax.

But, the amount having been thus fixed, the *lien* therefor necessarily, by the express terms of the statute, must be held to have attached as of the date of the distributions upon which said tax (including the penalty) was based. The order of the district court should be modified to so provide.

D. Point Four

Said district court erred in ordering that said claim of F. R. Kenney and said L. W. Wickes constitutes a lien upon the property described in said deed of trust and chattel mortgage prior and paramount to the lien of the State of California upon said property for licenses taxes due on account of motor vehicle fuel sold and delivered by said El Camino Oil Company, Ltd., subsequent to the tenth day of June, 1930, together with penalties thereon for delinquencies.

This point relates to the errors assigned as Numbers VI and XII in the assignments of error filed herein. (Tr. pp. 97-99.) Said assignment Number VI relates specifically to the priority of the lien of the chattel mortgage, over said tax lien, and assignment Number XII relates specifically to the priority of the lien of the deed of trust, over said tax lien. Since the same legal principles are involved as to each of said contract liens in this regard, said assignments have been combined into the foregoing single statement of the proposition presented herein.

Briefly stated, the proposition of the appellant presented under this point is that, even if it be

assumed that the claim of the foregoing contract creditors was secured by said chattel mortgage, and that said deed of trust is valid as against the State of California, and that the lien for penalties on taxes based on distributions from April 1, 1930, to June 10, 1930, attached subsequent to said tenth day of June, 1930, rather than as of the date of said distributions, still, in any event, the lien securing the claim of the State of California *in its entirety,* was nevertheless prior and paramount to any lien of said contract creditors. In other words, it is submitted that even the portion of the state's lien which attached subsequent, in point of time, to the recording of the lien of the contract creditors, is prior and paramount to any valid antecedent contract lien upon the property of the tax debtor.

It has never been disputed by the appellee that the legislature has the *power* to make a tax lien paramount to an antecedent contract lien. And, as is stated in *Guinn* vs. *McReynolds,* 177 Cal. 230, at 232 (1918).

> *"The priority need not be declared in express terms. It is enough if the intent to postpone contract liens appear by reasonable inference from the provisions of the act."* (Italics added.)

Therefore, the only question for determination herein, is whether the Legislature of the State of California has *exercised* this power in so far as the tax lien here in question is concerned.

In section 4 of the California Motor Vehicle Fuel License Tax Act, quoted hereinabove, it is specifically provided that said lien "shall have the effect of an execution duly levied against all property of the distributor, *and shall remain until the tax is paid or the property sold for the payment thereof.*" (Emphasis ours.) It is submitted that by this provision the legislature has clearly evidenced its intention to make the tax lien superior to *all* contract liens. No other possible construction can be given to said language and give any reasonable effect thereto. Thus, it does not appear how it would be possible for the tax lien to "remain until the tax is paid" if such lien is subject to an antecedent contract lien which might, of course, foreclose out any inferior lien. Nor is it disclosed how it would be possible to sell said property *for the payment of the taxes* if the tax lien is inferior to an antecedent contract lien, which tax lien might thus be wiped out before the property is ever sold for the taxes. For instance, if the property involved herein had already been sold under a proceeding to enforce the contract lien which the contract creditors claim is paramount, and the tax had not been paid nor the property sold for the payment thereof, then clearly, by the express terms of the statute, *the tax lien would remain notwithstanding such sale.* Yet it could *not* remain unless it were paramount to the earlier dated contract lien. On principle, then, the conclusion is inevitable that the legislature, by the provisions of said section 4, intended to and did

provide that the lien for motor vehicle fuel taxes should be paramount to earlier dated contract liens upon the property of the taxpayer.

In fact, this very construction has been placed upon these same words when used in relation to the *personal property* tax lien in California.

> *California Loan & Trust Co.* vs. *Weis,* 118 Cal. 489 (1897).

Section 3716 of the California Political Code, which was before the court in the cited case, then read as follows:

> "Every tax has the effect of a judgment against the person, and every lien created by this title has the force and effect of an execution duly levied against all property of the delinquent; the judgment is not satisfied nor the lien removed until the taxes are paid or the property sold for the payment thereof."

In 1930, section 4 of the California Motor Vehicle Fuel License Tax Act, provided in part as follows:

> " * * * Said tax shall be a lien upon all of the property of the distributor. It shall attach at the time of the delivery or distribution, subject to the tax, shall have the effect of an execution duly levied against all property of the distributor, and shall remain until the tax is paid or the property sold for the payment thereof * * * "

In the cited case the California Supreme Court held that said section 3716 of the Political Code

clearly indicated the legislative intention to make the tax lien paramount to even *antecedent* contract liens upon *real property* of the party owing *personal property taxes.*

The appellees will undoubtedly follow the course pursued by them in the court below, of claiming that any language favorable to the appellant which may be found in this decision is but dicta, relying upon the court's further reference to section 3788 of the California Political Code. In view of the importance of the cited case upon the question here involved, the court will undoubtedly want to read said case in its entirety. The appellant will not, therefore, burden the court with lengthy quotations therefrom. Suffice it to say that, in such reading the court will unquestionably be impressed with the fact that the California court was *not* merely expressing certain dicta, but was carefully considering all the statutory provisions pertinent to the question before them. They based their decision upon *both* statutory provisions (Pol. Code, secs. 3716 and 3788), and the mere fact that they stated that their construction of Political Code section 3716 was "*aided* so as to remove the need of interpretation by section 3788" does not mean that their decision was not based, at least in the first instance, upon their full consideration of the first of these sections.

In any event, whether the language in said case be decision or dicta, the fact remains that that is

the *only* construction which has been placed upon such language in California. It is wholly unreasonable, then, to assume that the California Legislature, in using this same language in section 4 of the California Motor Vehicle Fuel Tax Act, intended that it should be interpreted as might have been done by the courts of other states. Clearly, they must have intended to use said language in the only sense in which it has ever been construed by the California courts, whether such construction be by decision or dicta. Therefore, appellant will not encumber this brief with an analysis of the conflicting decisions upon this question, in *other* states. It is the law of *this* state with which we are here concerned. It is very apparent that the Legislature deliberately adopted, in the Motor Vehicle Fuel License Tax Act, the identical language which the California Supreme Court had held made the *personal property* tax lien paramount to antecedent contract liens upon the real property of the tax debtor. Their intention to make this license tax lien of the same effect as said personal property tax lien could not have been more clearly indicated.

Finally, this honorable court, as recently as January 18, 1937, in the case of *Berryessa Cattle Company* vs. *Sunset Pacific Oil Company (Sunset Oil Company, appellants,* vs. *The State of California, and Ray L. Riley, Controller of the State of California, appellees),* being No. 8182 before this

court, has squarely held that the lien of taxes such as those here in question is paramount to antecedent contract liens. This particular point was not discussed in the *opinion* of the court in that case, but the point was squarely raised, and argued to the court, and, in affirming the decision of the court below, this court necessarily was required to hold that the state's tax lien was paramount to the lien of the contract creditor (the appellant in said case) under an earlier dated deed of trust.

The decision herein, of the court below, should therefore be modified so as to order that the lien of the State of California, is, in any event, paramount to any antecedent contract lien which the individual claimants herein may have.

E. Conclusion

In conclusion, it is submitted that the order of the district court must be modified in each of the foregoing particulars. The chattel mortgage of June 6, 1930, was fully satisfied by the credit to which the El Camino Oil Company became entitled when the accounting was had between said company and the individual claimants, appellees herein. Therefore, no portion of the claim of said creditors should have been held secured by the lien of said chattel mortgage. The district court erred in ordering that the claim of said individual creditors was secured by the lien of said chattel mortgage.

The trust deed of June 7, 1930, was, as to the property described as Parcel II, merely an attempted mortgage of personal property, viz, of a certain leasehold interest of the El Camino Oil Company. It was not, however, executed in the manner required by law for mortgages of personal property. Said instrument was therefore invalid as against the State of California as tax creditor of said oil company. The district court erred in ordering that the claim of said individual creditors was secured by the lien of said deed of trust as a valid lien, as against the State of California, upon said property described therein as Parcel II.

The penalties which were added to the taxes assessed upon the basis of distributions of motor vehicle fuel by the El Camino Oil Company from April 1, 1930, to June 10, 1930, inclusive, were a lien upon the property of said company. The district court properly so held, but failed to order that said lien attached as of the dates of such distributions (the same as did the lien for the taxes to which said penalties were added), and consequently *prior in time* to the recording of the chattel mortgage and deed of trust relied upon by the individual claimants. The district court erred in failing to specify in its order the date as of which said lien for said penalties attached, and in failing to order that the lien of said penalties was prior and paramount to any lien of said chattel mortgage and trust deed.

Finally, and without regard to the determination made by the court upon the foregoing propositions, the tax lien of the State of California for even that portion of its claim which accrued subsequent in point of time to the recording of said chattel mortgage and deed of trust, is paramount to even valid liens which may have been created by said contractual encumbrances. In other words, even if the chattel mortgage was *not satisfied* by said accounting whereby the mortgagor became entitled to a credit in excess of the amount of said mortgage, but is an existing and valid lien, and even if said deed of trust was *not invalid* as against the State of California as to the personal property described therein as Parcel II, and even if the lien for the penalties upon the taxes based upon distributions of motor vehicle fuel from April 1, 1930, to June 10, 1930, inclusive, did *not attach* as of the dates of said distributions (the same as did the lien for the tax which was assessed upon the basis of said distributions), still, the *entire* tax lien of the State of California, is superior and paramount to even such *valid* contract liens, even though a portion of said tax lien is *subsequent in point of time* to said contract liens. The legislature of the State of California clearly expressed its intention that the lien for the taxes in question should be paramount to antecedent contract liens. There is no question as to the *power* of the legislature to so provide. It *exercised* this power by adopting language which

the California Supreme Court had previously held disclosed the intention to make the tax lien paramount to antecedent contract liens. The district court erred in ordering that that portion of the state's lien which attached *subsequent* to June 10, 1930, was inferior to any lien which the individual creditors may have acquired as against the state by recording said chattel mortgage and deed of trust on that date.

The order of the district court should be modified accordingly. It should be ordered that no portion of the claim of said individual creditors is secured by said chattel mortgage; and that, in any event, any such lien is inferior to the *entire* tax lien of the State of California. It should further be ordered that no portion of the claim of said individual creditors is, as against the State of California, secured by said deed of trust as upon the property described therein as Parcel II; and that, in any event, any such lien is inferior to the *entire* tax lien of the State of California. It should be further ordered that the lien for the penalty which was added to the taxes which were based upon distributions of motor vehicle fuel from April 1, 1930, to June 10, 1930, attached as of the dates of such distributions, and so were *prior in point of time,* and so superior to any lien of the contract creditors; and that, in any event the *entire* tax lien of the State of California is *paramount* to *any* lien of the contract creditors, even if such contract lien be earlier, in point of

time, than the tax lien of the state. Finally, and principally, it should be ordered that the tax lien of the state is paramount to even antecedent contract liens.

Respectfully submitted.

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